

COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION I
CIVIL ACTION NO. 05-CI-00459

COMMONWEALTH OF KENTUCKY,
OFFICE OF ATTORNEY GENERAL
Ex rel. Gregory D. Stumbo in his official
capacity as Attorney General of the
Commonwealth of Kentucky

PLAINTIFF

v.

BOARD OF DIRECTORS FOR THE
COMMONWEALTH
POSTSECONDARY EDUCATION
PREPAID TUITION TRUST FUND, et al.

DEFENDANTS

**THE FINANCE AND ADMINISTRATION
CABINET'S OBJECTION TO PLAINTIFF'S
MOTION FOR TEMPORARY INJUNCTION**

The "KAPT Fund" is the Commonwealth Postsecondary Prepaid Tuition Trust Fund. It was established by the General Assembly in 2000 for the stated purpose of protecting families against the rising costs of college tuition by allowing participants to pay their college tuition in advance at today's rates. In return for their KAPT investments, the KAPT beneficiaries receive tuition credits which they may redeem in the future to pay for their college tuition.

In December, 2004, the KAPT Board seized \$13.7 Million in abandoned property funds, which are general funds, to cover a projected actuarial deficit in the KAPT Fund. In the recently enacted Budget Bill the Legislature ordered that this money be returned to the General Fund before June 30, 2005. The money has not yet been returned. The Attorney General now challenges the constitutionality of (1) this

reclamation of public funds, and (2) the Budget Bill's prohibition against KAPT's future use of abandoned property funds.

The Attorney General moves for a preliminary injunction prohibiting the \$13.7 Million transfer from the KAPT Fund to the General Fund. His motion should be denied for numerous reasons. First, this case is entirely about money. Accordingly, the alleged harm is not irreparable, as there is an adequate remedy at law: restitution of the money. If the Attorney General wins this case, this Court can simply enter a judgment requiring the Commonwealth to transfer the \$13.7 Million from the General Fund back to the KAPT Fund. Second, the alleged harm is not immediate. There is absolutely no allegation, nor could there be, that KAPT will quit making tuition payments if the requested injunction is not entered. To the contrary, KAPT can fulfill all of its obligations during the pendency of this litigation, and far beyond, even if the \$13.7 Million transfer at issue is made. Third, the balancing of equities weighs strongly against the requested injunction. The challenged budget provisions were enacted to fund essential services of the Commonwealth that may go unfunded without the transfer. Fourth, the Attorney General has not shown a strong likelihood of success on the merits. It is unclear at this time whether he even has standing to bring this case.

ARGUMENT

It is well-settled Kentucky law that preliminary injunctions are "extraordinary relief," and are only warranted where [1] it is "clearly shown that one's rights will suffer immediate and irreparable injury pending trial", [2] the balance of equities is in favor of injunctive relief; and [3] there is a serious question presented. *Maupin v. Stansbury*, 575 S.W.2d 695, 698 (Ky. App. 1978). A remote possibility of some feared wrong in the future is not sufficient to support an award of a temporary

injunction. *Com. ex. rel Cowan v. Wilkinson*, 828 S.W.2d 610, 612 (Ky. 1992). The party seeking the injunction must demonstrate an urgent necessity for the relief requested. *Id.*

In this case, the Attorney General has not and cannot satisfy the three prongs of the *Maupin* test, and thus his motion should be denied.

I. The Attorney General Cannot Show an Immediate or Irreparable Harm.

It is a well-recognized rule that where the harm allegedly suffered by the moving party may be compensated by an award or restoration of money, the harm is not irreparable. *See Transamerica Insurance Finance Corp. v. North American Trucking Association*, 937 F.Supp. 630, 634 (W.D. Ky. 1996). Accordingly, preliminary injunctions are almost never entered in cases solely concerning money. In fact, the Finance and Administration Cabinet ("Finance Cabinet") can find no case where a state officials were enjoined from executing a statutorily mandated transfer of money because a statute's constitutionality was questioned. Courts and prior plaintiffs undoubtedly recognize that any unconstitutional transfer of money can be remedied by a court order.

Here, if this Court ultimately determines that the Budget Bill provisions in question are unconstitutional, it can order that any money transferred from the KAPT Fund to the General Fund be refunded to the KAPT fund. This is an adequate remedy, and there is nothing "immeasurable" about it. The beauty of money is that it can be measured with precision, and this case only involves money.

The Attorney General, however, argues that once the \$13.7 Million transfer is made to the General Fund, those funds are not recoverable "because the Respondents are clothed with sovereign immunity under Section 231 of the Kentucky Constitution" [Motion, p. 1]. In other words, it is the Attorney General's position that

this Court has the power to declare laws unconstitutional, but does not have the power to order unconstitutionally obtained money be refunded to its proper owner. This is nonsense. The Attorney General's suggestion that sovereign immunity would somehow preclude this Court from later ordering restitution is not supported by case law and is patently wrong. *See Prewitt v. Illinois Life Ins. Co.*, 123 Ky. 36, 93 S.W. 633 (Ky. 1906) (State Treasurer can be compelled to transfer a fund deposited with him by an insurance company); *Anderson v. State Highway Commission*, 252 Ky. 696, 68 S.W.2d 5 (Ky. 1934) (landowners' suit to enjoin public officials not "suit against Commonwealth" for purposes of Ky. Const. § 231); *City of Louisville v. Martin*, 284 Ky. 490, 144 S.W.2d 1034 (Ky. 1940) (suits to enjoin public officials regarding their official acts not barred by Ky. Const. § 231). Inherent in this Court's power of judicial review is the power to order money unconstitutionally obtained by the Commonwealth be returned to its proper owner. For example, if the Legislature were to pass an unconstitutional tax on tall people, and this Court were to strike it down, it surely would have the power to order those taxes refunded to those who paid them. The Commonwealth could not keep the illegally obtained money under the doctrine of sovereign immunity.

Nevertheless, *even if* the \$13.7 Million transferred to the General Fund is not recoverable, *if* the Court finds the provisions at issue unconstitutional, the KAPT program would again have access to the KAPT Reserve Fund, as well as the abandoned property funds,¹ and thus could simply claim another \$13.7 Million from those funds to

¹ Abandoned property funds are general fund dollars received primarily from the sale of lost property such as stock certificates, mutual funds and other securities. The original KAPT legislation provided that "Seventy-five percent (75%) of the balance of the
(continued...)"

cover what was transferred to the General Fund. According to the Actuarial Report attached as Exhibit A to the Complaint, there was a \$14,638,949.00 “aggregate surplus” in the KAPT Reserve Fund, and \$80 Million in the abandoned property funds – more than enough to cover the \$13.7 Million transfer to the General Fund [Actuarial Report, p. 2]. Therefore, the bottom line is that even if \$13.7 Million transfer pulls this money out of reach of this Court – which is an unreasonable hypothesis – the harm is still not irreparable.

The alleged harm is also not immediate. Noticeably absent from the Attorney General’s motion and supporting affidavits is any allegation that KAPT will default on any obligation to KAPT contract beneficiaries during the pendency of this litigation unless this injunction is entered. KAPT currently has assets totaling \$89,964,665.00 in its coffers, and can unquestionably meet all obligations during the pendency of this litigation and well beyond [Exhibit A to Complaint, p. 2]. The only reason the KAPT Board even tapped the abandoned property funds for \$13.7 Million in December, 2004, was to cover a projected long-term *actuarial* deficit – not because of any immediate or near-term inability to meet its tuition obligations.

Moreover, the Actuarial Report confirms that even if the \$13.7 Million transfer is made, and KAPT is denied any further access to the Reserve or to the abandoned property funds, the soundness of the program can be preserved by new enrollments without affecting those already in the program:

(...continued)

abandoned property funds shall be available for support of the [KAPT] fund.” KRS 393.015. The recently enacted Budget Bill terminates this requirement.

We have projected that if KAPT reopens enrollment with contract prices that include a 7.5% premium surcharge, the Program can eliminate the [\$13.7 Million] actuarial deficit in less than 10 years.

[Actuarial Report, p. 2]. That is an option that the KAPT Board has and can take to cure the actuarial deficit, rather than trying to rely on the use of public taxpayer funds.

The bottom line is that existing KAPT beneficiaries will not suffer any immediate harm, and probably will suffer no harm, even if the \$13.7 Million transfer at issue is made to the General Fund. Any future harm is purely speculative and capable of being avoided by application of the Actuary's 7.5% premium surcharge option. The Attorney General's contentions to the contrary are groundless.

II. The Balance of Equities Weighs Strongly Against The Injunction the Attorney General Seeks.

The Legislature mandated the \$13.7 Million transfer in question for one simple reason: there is an immediate need for this money in the General Fund to pay for essential services. KAPT, on the other hand, does not face an immediate, or even near term, budget deficit preventing it from covering all immediate and near-term liabilities. Rather, it faces an "actuarial deficit" – meaning that actuaries project, based upon their assumptions, that if \$13.7 Million is transferred out of the KAPT fund, it *might* face problems years from now. This is not, of course, an immediate harm.

Equity dictates against injunctive relief that pulls money away from the Commonwealth's immediate, essential needs, simply to protect against projected, speculative, actuarial deficits in the KAPT Fund that have not yet occurred, may never occur, and can be cured by future enrollments, a more favorable economy, or lower tuition rate increases. There is simply no ground to suggest that KAPT is in immediate

and irreparable financial straits, or is unable or unwilling to fulfill its obligations. The equities weigh strongly against the injunction the Attorney General seeks.

III. The Attorney General Cannot Show Abrogation of a Concrete Personal Right and his Substantive Arguments are Weak.

This motion for an injunction was filed on April 4, 2005 – only three days before the date of the scheduled hearing on April 7, 2005.² Accordingly, it is impossible for Defendants to prepare an extensive brief or argument addressing all aspects of this case. But even at this early date it appears that the Attorney General's claims will fail.

First, it appears that the Attorney General may not even have standing to bring his claim. The Attorney General alleges that he is the “chief law officer” of the Commonwealth [Complaint ¶ 3]. As such, his job is to *enforce* the laws duly enacted by the Legislature and the Governor, including the recently enacted Budget Bill. It is not his job to challenge them. Moreover, the Attorney General did not enter into any contract with the Commonwealth for prepaid tuition. It is doubtful whether he can actually step into the shoes of those individuals who purchased KAPT contracts and assert what amounts to a breach of contract claim on their behalf. These private individuals appear to be the only people who possibly have standing to bring this case, as they are the only ones who may have concrete personal rights being affected. *See Maupin*, 575 S.W.2d at 698 (a party seeking an injunction “must first allege possible abrogation of a concrete personal right”).³

² This is a violation of Franklin Circuit Rule No. 8, which requires that “Notice, together with motion and copies, shall be filed with the Circuit Clerk and served upon the parties not less than five (5) business days before the date of the hearing.”

³ Contrast this case to *Haydon Bridge Company, Inc. et al. v. Ernie Fletcher, et al.*, No. 03-CI-01547, which is now pending in this Court's other division, where several actual individual employers – not the Attorney General – are seeking to vindicate their alleged

(continued...)

Second, regardless of the Attorney General's standing, this case is nowhere close to being ripe. The Commonwealth has committed to pay the tuition of beneficiaries of KAPT contracts. It has not missed a single payment, and there is no immediate threat that it will do so. The Finance Cabinet respectfully submits that there is no impairment or breach of contract action until KAPT misses a tuition payment – something that has not and will almost certainly never happen.

The Attorney General may claim that there is a “threat” that a payment might be missed in the future. The only evidence of a “threat,” however, is the actuarial report attached to the Complaint that shows a speculative “actuarial deficit” of \$13.7 Million at some point well in the future. But the actuarial predictions may never occur. Moreover, the actuary stated that new enrollments may erase the actuarial deficit without the help of the \$13.7 Million.

The Kentucky Supreme Court dealt squarely with this issue in *Jones v. Board of Trustees of Kentucky Retirement Systems*, 910 S.W.2d 710 (Ky. 1995). There, the Kentucky Employee Retirement System (“KERS”) sued over the Legislature’s failure to make a state contribution to the program recommended by the actuary as necessary for the long-term stability of the program. The KERS Board claimed that the 1992 Budget Bill usurped its authority to set actuarially sound employer contribution rates. As in the instant case, the Board argued that the failure to fund the program as the Board wanted it

(...continued)

personal rights as relates to certain statutorily-mandated transfers from the Workers' Compensation Special Fund to the General Fund.

funded impaired KERS members' contract rights under the state and federal constitutions. *Id.* at 711-712.

While the Circuit Court accepted that argument, the Supreme Court had little problem reversing. The high court held that unless and until the contracts with the individual employees were breached by failure to pay them their required benefits, there was no injury, and any claim was premature. The Court held that the Board had shown no existing impairment of the employee's contract rights. *Id.* at 713-715. Here we have the same situation. KAPT has not failed to pay any tuition benefits, there is no immediate threat of such failure, and thus there is no existing impairment of the KAPT contracts.

Third, the Attorney General claims that the General Assembly had no authority to reclaim the \$13.7 Million transferred from the abandoned property funds to the KAPT fund, as these funds have been "commingled" with allegedly "private" funds, and therefore have become untouchable [Complaint ¶ 18]. This argument also fails. KAPT participants specifically agreed in the KAPT Contract that all money in the KAPT Fund, including money they paid into the Fund, is "public" in nature:

8.02 Public Funds. Assets of the Fund shall constitute public funds of the Commonwealth and may be invested in any instrument, obligation, security, or other property which constitutes legal investments for the investment of public funds in the Commonwealth which are deemed most appropriate by the Board.

[Exhibit F to Complaint] (emphasis added). Accordingly, the KAPT Fund is composed entirely of "public" funds – it contains no "private" funds as the Attorney General alleges. Furthermore, the version of KRS 164.701(4) in effect in when KAPT withdrew \$13.7 from the abandoned property funds in December, 2004, specifically designated all KAPT funds as public. Nevertheless, even if the money paid by KAPT participant were

to be deemed “private” in nature, the fact that “public” and “private” funds are commingled does not mean they are untouchable. Kentucky’s Supreme Court specifically held that where public and private funds are commingled, public funds can be transferred to the General Fund so long as the source of funding can be differentiated:

Because the General Assembly has no authority to transfer private funds to the general fund, the transfer of money from agencies in which public funds and private employee contributions are commingled, *and cannot be differentiated*, is unconstitutional.

Armstrong v. Collins, 709 S.W.2d 437, 447 (Ky. 1986) (emphasis added).

Here the \$13.7 Million originating in the abandoned property funds most certainly can be differentiated from the allegedly private contributions from KAPT participants. In fact, the KAPT’s managers can, and do, differentiate between the contributions made by the 8,900 KAPT participants:

Payments toward the purchase of a KAPT contract are accounted for *separately* by beneficiary and the purchaser is provided an annual account statement.

[Complaint, ¶ 24]. Surely if KAPT’s managers can differentiate between thousands of allegedly “private” contributions, they can differentiate between a \$13.7 Million “public” contribution and the allegedly “private” contributions.

The Attorney General tries to create the appearance of hopeless commingling through the affidavit of Clinton G. Long, an investment consultant at Fifth Third Bank. All that Mr. Long states, however, is that the allegedly public and private funds were commingled and then used to purchase securities [Long affidavit, ¶¶2-4]. But this fact does not *ipso facto* mean that the funds cannot be differentiated. Mr. Long does not go that far. For example, imagine that a commingled fund has \$100 – \$75 from private sources, \$25 from public sources. The \$100 is then used to buy a share of stock,

and in three years is worth \$200. Looking to the source of the seed money, one can differentiate between the portion of the fund that is private and that which is public: \$150 is private, and \$50 is public. The fact that the money was pooled to purchase a security does not mean that one cannot differentiate the money through basic accounting principles.

Moreover, the Office of the Attorney General is on record as opining that "[t]he assets of KAPT are deemed 'public funds of the Commonwealth,'" and that KAPT funds also may be pooled with any other eligible investment of the Commonwealth. *See* OAG 01-3. Thus, the Attorney General's argument that funds originating in the abandoned property funds, when pooled with KAPT funds, become inextricably commingled, is a Johnny-come-lately position which runs afoul of the Office's previous OAG. The authority to pool KAPT funds and other public monies is proper.

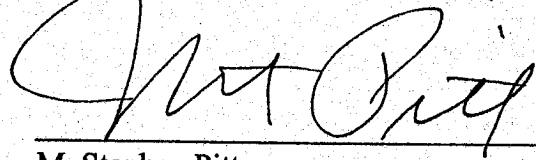
Nonetheless, even if the Attorney General shows a likelihood of success on the merits, he still has failed to demonstrate the immediate and irreparable harm necessary to obtain the requested injunction. This Court can always order any improperly transferred funds be transferred back at a later time if that proves necessary.

CONCLUSION

Attorney General Stumbo has not and cannot provide this Court any reason to enjoin the Defendants from executing the statutorily required transfer of \$13.7 Million from the KAPT Fund to the General Fund. He has not and cannot show the immediate and irreparable injury necessary to obtain the extraordinary relief he requests. Moreover, the equities weigh completely in Defendants' favor, and the Attorney General has not shown a substantial likelihood that his claims will succeed. It is questionable whether he even has standing to bring this suit. Accordingly, Defendants respectfully ask

this Court to deny the Attorney General's Motion for Temporary Injunction, and allow this case to proceed along its normal course.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "M. Stephen Pitt", written over a horizontal line.

M. Stephen Pitt
Christopher W. Brooker
WYATT, TARRANT & COMBS, LLP
500 West Jefferson Street, Suite 2800
Louisville, Kentucky 40202-2898
502.589.5235

Counsel for Commonwealth of Kentucky,
Finance and Administration Cabinet